Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Message Text

UNCLASSIFIED

PAGE 01 LONDON 02735 01 OF 05 161856Z
ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 INRE-00 SSO-00
NSCE-00 USIE-00 AID-05 CIAE-00 EB-08 FRB-01 INR-07
NSAE-00 XMB-04 OPIC-06 SP-02 CIEP-02 LAB-04 SIL-01
OMB-01 NSC-05 SS-15 STR-04 CEA-01 EURE-00 ABF-01
AGRE-00 /112 W
----------161918Z 067370 /42
O R 161844Z FEB 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 0702
TREASURY DEPT WASHDC IMMEDIATE
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY DUBLIN
AMEMBASSY NEW DELHI
AMEMBASSY PARIS
AMEMBASSY ROME
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AMCONSUL BELFAST
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USMISSION OECD PARIS
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UNCLAS SECTION 01 OF 05 LONDON 02735

DEPARTMENT PASS FEDERAL RESERVE BOARD

TREASURY FOR DONALD E. SYVRUD, OASIA

E.O. 11652: N/A
TAGS: ECON, UK
SUBJECT: ECONOMIC DEVELOPMENTS - PERIOD, FEB 9 - FEB 15

SUMMARY: THIS HAS BEEN A SOBERING WEEK IN THE U.K. THE
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PAGE 02 LONDON 02735 01 OF 05 161856Z

CURRENT ACCOUNT RELAPSED INTO SUBSTANTIAL DEFICIT IN
JANUARY. DECEMBER'S INDUSTRIAL PRODUCTION AND JANUARY'S
RETAIL SALES REMAINED FLAT. THE MARKETS IN FOREIGN EX-
CHANGE AND GILTS REVERSED THEIR SURGE. THE CENTRAL GOV-
ERNMENT BORROWING REQUIREMENT WAS ENCOURAGINGLY LOW FOR
THE FIRST 10 MONTHS OF THE FINANCIAL YEAR.
END SUMMARY

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

1. JANUARY'S CURRENT ACCOUNT DEFICIT ROSE TO 345 MILLION POUNDS FROM A REVISED DECEMBER DEFICIT OF 15 MILLION POUNDS. THE DEFICIT ON VISIBLE TRADE IS ESTIMATED TO BE 545 MILLION POUNDS, THE LARGEST MONTHLY DEFICIT ON RECORD. OFFICIALS EXPLAINED THIS TURNAROUND LARGELY IN TECHNICAL TERMS AS FAULTY SEASONAL ADJUSTMENT IN THE FACE OF AN ABNORMALLY LOW LEVEL OF ECONOMIC ACTIVITY DURING CHRISTMAS. THE ADVERSE MOVEMENTS IN TRADE WERE SO LARGE, WITH IMPORT VOLUME INCREASING 16.2 PERCENT AND EXPORT VOLUME DECLINING BY 1.6 PERCENT, THAT CONCERN NONETHELESS WAS EXPRESSED IN THE MARKETS AND IN THE PRESS. (SEE LONDON 2623)

2. RETAIL SALES VOLUME IN JANUARY WAS VIRTUALLY UNCHANGED FROM THE LEVEL ESTABLISHED IN THE SECOND HALF OF 1976, ACCORDING TO THE SEASONALLY ADJUSTED SERIES RELEASED BY THE DEPARTMENT OF INDUSTRY FEBRUARY 14. THE VALUE OF RETAIL SALES, THOUGH NOT COMPARABLE WITH THE VOLUME INDEX, CLEARLY REFLECTS VERY LITTLE ELSE BUT PRICE MOVEMENTS AT THIS TIME.

	RETAIL SALES	
	VOLUME	VALUE
	SEASONALLY ADJUSTED	NOT SEASONALLY ADJUSTED
	1971 EQUALS 100	PERCENT CHANGE OVER A YEAR EARLIER
1975 3RD QTR	105.4	18
4TH QTR	105.7	15
1976 1ST QTR	107.3	15

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2ND QTR	107.6	12
3RD QTR	108.9	15
4TH QTR	108.5	16
JANUARY	110.2	16
OCTOBER	108.1	16
NOVEMBER	109.2	17
DECEMBER	108.3	16
1977 JANUARY	108.0 PROVISIONAL	14

ALTHOUGH THERE ARE MANY SMALL CONTRIBUTING FACTORS TO THIS PATTERN, THE LARGEST INFLUENCE IS PROBABLY THE DECLINING REAL PERSONAL INCOME OF CONSUMERS. MOST FORECASTERS EXPECT A DECLINE IN CONSUMER EXPENDITURE DURING 1977 AS A

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Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

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PAGE 01 LONDON 02735 02 OF 05 161904Z
ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 INRE-00 SSO-00
NSCE-00 USIE-00 AID-05 CIAE-00 EB-08 FRB-01 INR-07
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O R 161844Z FEB 77
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USMISSION OECD PARIS
USDEL MTN GENEVA
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UNCLAS SECTION 02 OF 05 LONDON 02735

RESULT OF A CONTINUING FALL IN REAL INCOME, IN WHICH
EVENT RETAIL SALES MAY BE EXPECTED TO SHOW A MILD DECLINE
OVER THE YEAR.

3. THE CENTRAL GOVERNMENT BORROWING REQUIREMENT FOR THE
FIRST 10 MONTHS OF THE CURRENT FINANCIAL YEAR WAS MADE
AVAILABLE FEBRUARY 2, SHOWING A SMALLER THAN ANTICIPATED
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PAGE 02 LONDON 02735 02 OF 05 161904Z

DEFICIT OF 3,820 MILLION POUNDS COMPARED WITH 5,282 MIL-
LION IN THE COMPARABLE PERIOD OF THE 1975/76 FINANCIAL
YEAR. A SUMMARY OF THE ACCOUNTS FOLLOWS:

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

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IN MILLIONS OF POUNDS

CONSOLIDATED FUND	1975-76 OUTTURN	BUDGET FORECAST	1 APR-31 JAN 1976	1977	JANUARY 1976	1977
REVENUE	29,417	33,197	24,417	28,193	4040	4742
EXPENDITRE.	36.047	39,915	29,699	32.013	3573	3336
DEFICIT MET FROM NAT'L LOANS FUND	-6,630	-6,718	-5,282	-3,820	467	1406
OTHER NATIONAL LOANS FUND TRANSACTIONS (1)						
RECEPITS	3573	4900	2906	3400	464	252
PAYMENTS	6296	8932	5021	4530	663	657
TOTAL NET BORROWING BY NAT'L LOANS FUND	-9353	-10750	-7397	-4950	268	1001
OTHER FUNDS AND CENTRAL GOVERNMENT BORROWING REQUIREMENT	-8807	-10,426	-6898	-3937	504	1235

(1) EXCLUDING NATIONAL DEBT AND OTHER TRANSACTIONS CONCERNED WITH THE FINANCING OF THE BORROWING REQUIREMENT.

REVENUE AND EXPENDITURE LEVELS ARE SUBJECT TO LARGE SEASONAL VARIATION. JANUARY, IN PARTICULAR, RUNS SEASONALLY HIGH TAX REVENUES. SMALLER DEFICIT HOWEVER CANNOT BE ACCOUNTED FOR BY SEASONAL INFLUENCES ALONE. CUSTOMS AND EXCISE TAXES ARE HIGHER THAN EXPECTED WHICH MAY BE ATTRIBUTED TO THE UNUSUALLY STRONG PRE-CHRISTMAS TOURIST BOOM. THE "OTHER CENTRAL GOVERNMENT FUNDS AND ACCOUNTS,"

WHICH INCLUDES THE NATIONAL INSURANCE FUND, IS RUNNING A SURPLUS OF 1013 MILLION POUNDS SO FAR THIS FINANCIAL YEAR COMPARED WITH 499 MILLION IN THE SAME PERIOD LAST YEAR. FOR FY 1975/76 AS A WHOLE, THIS ACCOUNT HAD A SURPLUS OF 546 MILLION POUNDS. A SURPLUS OF 324 MILLION POUNDS WAS ORIGINALLY ESTIMATED FOR THIS ENTIRE FINANCIAL YEAR.

LOANS FROM THE NATIONAL LOANS FUND ARE VERY LOW, AMOUNTING TO 766 MILLION POUNDS IN THE FIRST 10 MONTHS OF THE 1976/77 FINANCIAL YEAR COMPARED WITH 2115 MILLION FOR THE SAME PERIOD IN FY 1975/76. THESE LOANS, WHICH ARE TO THE NATIONALIZED INDUSTRIES, PUBLIC CORPORATIONS, AND LOCAL AUTHORITIES INTER ALIA, TOTALLED NET 2736 MILLION POUNDS IN 1975/76 AND WERE BUDGETED TO TOTAL 4032

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

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MILLION POUNDS IN 1976/77. THERE ARE SEVERAL REASONS FOR THIS LOW LEVEL. CENTRAL GOVERNMENT LENDING TO THE REST OF OF THE PUBLIC SECTOR HAS BEEN REDUCED IN CONSEQUENCE OF THE USE OF
PUBLIC SECTOR FOREIGN CURRENCY BORROWING UNDER THE EXCHANGE GUARANTEE SCHEME, BORROWINGS WHICH PARTLY SUBSTITUTE FOR CENTRAL GOVERNMENT FINANCE. LOCAL AUTHORITIES CAN BORROW SHORT-TERM IN THEIR OWN NAME, AND ARE LIKELY TO HAVE INCREASED SUCH BORROWING IN A PERIOD OF FALLING INTEREST RATES IN ORDER TO POSTPONE BEING LOCKED INTO THE GOVERNMENT'S MEDIUM-TERM FINANCE AT HIGHER INTEREST COSTS.

THE PRESS HAS SPECULATED THAT THESE FIGURES PORTEND A PUBLIC SECTOR BORROWING REQUIREMENT (PSBR) FOR THE CURRENT FINANCIAL YEAR OF BETWEEN 10 AND 10-1/2 BILLION POUNDS RATHER THAN THE 11.2 BILLION OOUNDS FORECAST BY THE TREASURY IN DECEMBER. IT HAS REPORTED FURTHER THAT THE TREASURY IS CURRENTLY REVISING DOWNWARD ITS FORECAST PSBR FOR BOTH THE CURRENT AND THE APPROACHING FINANCIAL YEARS.

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PAGE 04 LONDON 02735 02 OF 05 161904Z

4. THERE WERE NO SIGNIFICANT GAINS IN INDUSTRIAL PRODUCTION IN DECEMBER OVER THE REST OF 1976. THE SEASONALLY ADJUSTED INDEX FOR ALL INDUSTRIES STOOD AT 102.8 IN DECEMBER COMPARED WITH 102.9 FOR THE 4TH QUARTER OF 1976

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PAGE 01 LONDON 02735 03 OF 05 161904Z
ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 INRE-00 SSO-00
NSCE-00 USIE-00 AID-05 CIAE-00 EB-08 FRB-01 INR-07
NSAE-00 XMB-04 OPIC-06 SP-02 CIEP-02 LAB-04 SIL-01
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O R 161844Z FEB 77

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

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TO SECSTATE WASHDC IMMEDIATE 0704
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INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
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AMCONSUL EDINBURGH
USMISSION EC BRUSSELS
USMISSION OECD PARIS
USDEL MTN GENEVA
USDOC WASHDC

UNCLAS SECTION 03 OF 05 LONDON 02735

AND 102.2 FOR THE YEAR AS A WHOLE. THE MONTHLY INDEX
IS ERRATIC, BEING SUBJECT TO THE SAME FAULTY SEASONAL
ADJUSTMENTS, UNUSUAL STOCKING SHIFTS, ETC. THAT BEDEVIL
OTHER MONTHLY STATISTICS, BUT OVER THE YEAR DISPLAYS AN
UNDENIABLY FLAT PROFILE. INDUSTRIAL PRODUCTION GROWTH IS
IN FACT INFLATED BY NORTH SEA OIL PRODUCTION, WHICH ROSE
7.2 PERCENT IN THE FINAL QUARTER OF 1976. INDUSTRIAL AND
UNCLASSIFIED

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PAGE 02 LONDON 02735 03 OF 05 161904Z

MANUFACTURING PRODUCTION LEVELS REMAIN BELOW LEVELS
RECORDED IN THE FIRST QUARTER OF 1975.
INDUSTRIAL PRODUCTION 1970 EQUALS 100 SEASONALLY ADJUS.

	ALL INDUSTRIES	TOTAL MANUFACTURING
1975 1ST QTR	104.7	106.1
2ND QTR	100.3	100.5
3RD QTR	99.6	99.7
4TH QTR	100.4	100.4
1976 1ST QTR	102.1	102.0
2ND QTR	102.4	103.5
3RD QTR	101.5	103.4
4TH QTR	102.9	104.2
JULY	101.4	103.6
AUGUST	100.6	102.4
SEPTEMBER	102.4	104.2
OCTOBER	102.8	104.8
NOVEMBER	103.1	104.5
DECEMBER	102.8	103.2

SOURCE: CENTRAL STATISTICAL OFFICE

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

PRIME MINISTER CALLAGHAN COMMENTED UPON THE INDUSTRIAL PRODUCTION INDEX AS WELL AS THE RECENTLY RELEASED JANUARY CURRENT ACCOUNT STATISTICS. QUOTE...REGARDING GENERAL INDICATORS, I NOTE THAT MANUFACTURING INDUSTRY OUTPUT IS RISING AND THAT IS SOMETHING, I DARE SAY, WE ARE ALL PLEASED ABOUT. INDUSTRIAL PRODUCTION AS A WHOLE WAS 1.5 PERCENT HIGHER IN THE LAST 3MONTHS THAN THE PREVIOUS 3 MONTHS. THERE ARE SPECIAL REASONS FOR THAT. I NEVER BE-LIEVE IN OVERCLAIMING ON THESE MATTERS. BUT IF WE TAKE THE BALANCE OF PAYMENTS STATISTICS, THE LEVEL OF INFLA-TION OVER THE NEXT 12 MONTHS, AND THE LEVEL OF GROWTH AND EXPORTS, IT IS PROBABLY TRUE TO SAY THAT WE ARE MOVING INTO THE RIGHT DIRECTION--NOT FAST ENOUGH YET AND THERE IS MUCH MORE TO BE DONE. UNQUOTE

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5. THE DISCUSSIONS BETWEEN THE GOVERNMENT AND THE TUC OVER THE THIRD ROUND OF INCOMES POLICY ARE ENCOUNTERING DIFFICULTIES. THERE HAVE BEEN INCREASING DEMANDS FOR A RETURN TO FREE COLLECTIVE BARGAINING AND A GROWING RELUC-TANCE TO SETTLE PAY PROVISIONS PRIOR TO THE PRESENTATION OF THE BUDGET. LAST YEAR THE GOVERNMENT EFFECTED A TAX DECREASE IN PARTIAL COMPENSATION FOR FOREGONE WAGES OF A PAY RESTRAINT POLICY, AND HELD THE SIZE OF THE TAX CUT OPEN UNTIL THE DEGREE OF WAGE RESTRAINT BECAME KNOWN. (SEE LONDON 2492 AND LONDON 2680)

6. STERLING WAS BUFFETTED THIS WEEK IN THE FOREIGN EX-CHANGE MARKETS; THE RATIONALE BEING DOMESTIC WEAKNESS AND THE EXTERNAL STRENGTH OF OTHER CURRENCIES. FROM THE $1.7175 RANGE LAST WEEK, STERLING FELL STEADILY CLOSING AT $1.6970 ON MONDAY, FEBRUARY 14, AND THEN RECOVERING TO ABOVE $1.70 AFTER CONSIDERABLE BANK OF ENGLAND ACTIVITY IN SHORT-DATED FORWARDS, WHICH WIDENED APPRECIABLY.

ONE SENIOR FOREIGN EXCHANGE DEALER SAID THE EUPHORIC BUBBLE HAS BURST. PRESSURES TO SELL STERLING HAVE BEEN GENERATED ORINCIPALLY BY TRADE UNION AGITATION OVER THE THIRD STAGE OF INCOMES POLICY. ALSO CITED WAS LAB-OR UNREST AT LEYLAND, INDICATIONS THAT PRICE INFLATION MAY

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Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

NNN

UNCLASSIFIED

PAGE 01 LONDON 02735 04 OF 05 161910Z
ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 INRE-00 SSO-00
NSCE-00 USIE-00 AID-05 CIAE-00 EB-08 FRB-01 INR-07
NSAE-00 XMB-04 OPIC-06 SP-02 CIEP-02 LAB-04 SIL-01
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O R 161844Z FEB 77
FM AMEMBASSY LONDON
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AMCONSUL EDINBURGH
USMISSION EC BRUSSELS
USMISSION OECD PARIS
USDEL MTN GENEVA
USDOC WASHDC

UNCLAS SECTION 04 OF 05 LONDON 02735

CONTINUE TO RISE BEFORE IT RESUMES A DECLINE IN THE
RATE OF INCREASE, EC PRESSURES FOR DEVALUATION OF THE
GREEN POUND, WHICH WOULD PUT FURTHER PRESSURE ON UK
PRICES, AND THE POOR JANUARY TRADE FIGURES. IN ADDITION,
WITH TALK OF DM AND YEN APPRECIATION, THERE HAS BEEN SUB-
STANTIAL SWITCHING FROM STERLING INTO OTHER CURRENCIES--
PARTICULARLY THE DM VIA THE DOLLAR. FOREIGN EXCHANGE
UNCLASSIFIED

UNCLASSIFIED

PAGE 02 LONDON 02735 04 OF 05 161910Z

DEALERS ESTIMATE THE BANK OF ENGLAND'S NEW INTER-
VENTION ZONE (OPERATING ON BOTH SIDES OF THE MARKET) IN
THE$1.69 -$1.71 RANGE, WITH A FURTHER GRADUAL DECLINE
IN THE RATE TERMED HIGHLY PROBABLE.

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

7. INTEREST RATES IN THE MONEY MARKET WERE STEADY THROUGH MOST OF THE WEEK OF FEBRUARY 8-15, AS THE BANK OF ENGLAND GAVE EXCEPTIONALLY LARGE ASSISTANCE TO THE DISCOUNT HOUSES. BY TUESDAY, FEBRUARY 15, HOWEVER' THERE WERE SHARP FALLS IN THE SHORTEST INTEREST RATES WHILE THE LEVEL OF BANK ASSISTANCE TO THE DISCOUNT HOUSES HAD BEEN PERHAPS HALVED. WEDNESDAY, FEBRUARY 16, HOWEVER, IS A BANK MAKE UP DAY; CALL MONEY LENT BY BANKS TO THE DISCOUNT HOUSES MAY HAVE INCREASED AS SUCH LOANS ARE CONSIDERED AS RESERVE ASSETS IN MEETING SOME RESERVE REQUIREMENTS.

PRICES OF GILTS MOVED ERRATICALLY EARLY IN THE WEEK, ALTHOUGH SHOWING SOME DOWNWARD DRIFT. ON MONDAY, FEBRUARY 14, THE MARKET IN CONCERT WITH THE FALL IN STERLING BROKE SHARPLY, LOSING OVER A POINT IN THE FIRST HALF HOUR OF TRADING. THE MARKET THEN TRADED UNEASILY UNTIL JANUARY CURRENT ACCOUNT DEFICIT FIGURES WERE RELEASED, WHEN AGAIN IN CONCERT WITH THE FOREIGN EXCHANGE MARKET, PRICES FELL SHARPLY. THE MARKET RECOVERED ON TUESDAY AND WEDNESDAY, HELPED BY THE EASIER CONDITIONS IN THE MONEY MARKET, TO SHOW LOSSES ON THE WEEK OF AROUND 1/2 POINT IN THE SHORTS AND 1-1/2 POINTS IN THE LONGS.

8. EXCHANGE RATE AND GOLD

DATE	EFFECTIVE EXCHANGE RATE ($)	DEPRECIATION (PERCENT)	GOLD ($)
2/9	1.7175	42.8	136-5/8
2/10	1.7160	42.8	135-5/8
2/11	1.7125	43	135-1/8

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2/14	1.6970	43.6	136-3/8
2/15	1.7045	43.4	135-7/8

CHANGE 2/8-2/15
DOWN 0.0115 WIDEN 0.6 UP 1-1/8

9. FORWARD DISCOUNT ON STERLING

DATE	1 MONTH	3 MONTHS	6 MONTHS
2/9	1.15	3.48	5.98
2/10	1.12	3.48	6.10
2/11	1.22	3.72	6.65
2/14	1.38	3.98	7.15
2/15	1.60	4.40	7.55

CHANGE 2/8-2/15 0.47 WIDEN 0.95 WIDEN 1.65 WIDEN

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

UNCLASSIFIED

NNN

UNCLASSIFIED

PAGE 01 LONDON 02735 05 OF 05 161909Z
ACTION EUR-12

INFO OCT-01 EA-09 NEA-10 IO-13 ISO-00 INRE-00 SSO-00
NSCE-00 USIE-00 AID-05 CIAE-00 EB-08 FRB-01 INR-07
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O R 161844Z FEB 77
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USMISSION OECD PARIS
USDEL MTN GENEVA
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UNCLAS SECTION 05 OF 05 LONDON 02735

ALL FIGURES IN CENTS

10. EURODOLLAR INTEREST RATES

DATE	1 MONTH	3 MONTHS	6 MONTHS
2/9	4-3/4	5	5-1/2
2/10	4-3/4	5	5-1/2
2/11	5	5-1/8	5-5/8

UNCLASSIFIED

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PAGE 02 LONDON 02735 05 OF 05 161909Z

2/14	4-3/4	5-1/8	5-5/8

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

2/15 4-3/4 5-1/8 5-5/8
CHANGE 2/8-2/15 UNCHANGED UP 1/8 UP 1/8

11. 3-MONTH LONDON INTERBANK - EURODOLLAR INTEREST RATE
DIFFERENTIAL
DATE
2/9 6-31/32
2/16 7-1/16
2/11 6-13/16
2/14 7-1/16
2/15 7
CHANGE 2/8-2/15 NARROWED 1/8

12. STERLING CERTIFICATES OF DEPOSIT

DATE	1 MONTH	3 MONTHS	6 MONTHS
2/9	12-5/32	11-11/16	11-7/16
2/10	12-1/16	11-11/16	11-7/16
2/11	12-1/16	11-15/16	11-11/16
2/14	11-31/32	11-23/32	11-1/2
2/15	11-5/8	11-9/16	11-1/2

CHANGE 2/8-2/15
DOWN 17/32 DOWN 1/8 DOWN 1/16

L3. THE MINIMUM LENDING RATE REMAINED AT 12 PERCENT AS THE BANK OF ENGLAND CONTINUED TO SUSPEND ITS NORMAL DETERMINATION. THE TREASURY BILL RATE FELL BY 0.0590 PERCENT TO 11.1696 PERCENT AT FRIDAY'S TREASURY BILL AUCTION, WHICH WOULD HAVE IMPLIED A MINIMUM LENDING RATE OF 11-3/4 PERCENT IF THE BANK HAD NOT SET ASIDE ITS FORMULA. BIDS AT 1093.29 MILLION POUNDS WERE RECEIVED FOR THE 300 MILLION POUNDS TENDERED. THIS WEEK 300 MILLION POUNDS WILL BEOFFERED EXACTLY MATCHING THE AMOUNT MATURING.
ARMSTRONG

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Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009

Message Attributes

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Disposition Approved on Date:
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Executive Order: N/A
Errors: N/A
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Office: ACTION EUR
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Retention: 0
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Review Content Flags:
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Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
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Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3308162
Secure: OPEN
Status: NATIVE
Subject: ECONOMIC DEVELOPMENTS - PERIOD, FEB 9 - FEB 15 SUMMARY: THIS HAS BEEN A SOBERING WEEK IN THE U.K. THE UNCLASSIFIED
TAGS: ECON, UK
To: STATE TRSY
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